

**REPORT OF THE AUDIT OF THE
FORMER SIMPSON COUNTY
SHERIFF'S SETTLEMENT - 2002 TAXES**

January 5, 2003



EDWARD B. HATCHETT, JR.
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EXECUTIVE SUMMARY

**AUDIT EXAMINATION OF THE
FORMER SIMPSON COUNTY
SHERIFF'S SETTLEMENT - 2002 TAXES**

January 5, 2003

The Auditor of Public Accounts has completed the audit of the former Simpson Sheriff's Settlement - 2002 Taxes as of January 5, 2003. We disclaimed an opinion on the financial statement taken as a whole, because the Sheriff did not return a signed management letter.

Financial Condition:

The former Sheriff collected taxes of \$5,670,247 for the districts for 2002 taxes, retaining commissions of \$206,634 to operate the Sheriff's office. The former Sheriff distributed taxes of \$5,456,201 to the districts for 2002 Taxes. Taxes of \$1,133 are due to the districts from the former Sheriff and refunds of \$839 are due to the former Sheriff from the taxing districts.

Report Comments:

- The Former Sheriff Should Have Required Depository Institutions To Pledge Or Provide Additional Collateral Of \$686,306 To Protect Deposits
- The Former Sheriff Should Have Deposited Funds Intact On A Daily Basis
- Lacks Adequate Segregation Of Duties

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EDWARD B. HATCHETT, JR.
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Paul E. Patton, Governor

Gordon C. Duke, Secretary

Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Jim Henderson, Simpson County Judge/Executive

Honorable R. E. "Gene" Starks, Simpson County Sheriff

Honorable Joe Palma, Former Simpson County Sheriff

Members of the Simpson County Fiscal Court

Independent Auditor's Report

We were engaged to audit the former Simpson County Sheriff's Settlement - 2002 Taxes as of January 5, 2003. This tax settlement is the responsibility of the former Simpson County Sheriff.

As described in Note 1, the Sheriff's office prepares the financial statement on a prescribed basis of accounting that demonstrates compliance with the modified cash basis and laws of Kentucky, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

The former Simpson County Sheriff, Joe Palma, did not return a signed management representation letter to us. These representations are a required part of the audit.

Since the former Sheriff did not provide us with the written representations referred to above, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on this financial statement.

In accordance with Government Auditing Standards, we have also issued our report dated June 25, 2003, on our consideration of the former Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report.



To the People of Kentucky

Honorable Paul E. Patton, Governor

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Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Jim Henderson, Simpson County Judge/Executive

Honorable R. E. "Gene" Starks, Simpson County Sheriff

Honorable Joe Palma, Former Simpson County Sheriff

Members of the Simpson County Fiscal Court

We present the accompanying comments and recommendations, included herein, which discusses the following report comments:

- The Former Sheriff Should Have Required Depository Institutions To Pledge Or Provide Additional Collateral Of \$686,306 To Protect Deposits
- The Former Sheriff Should Have Deposited Funds Intact On A Daily Basis
- Lacks Adequate Segregation Of Duties

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Ed Hatchett", with a stylized flourish at the end.

Edward B. Hatchett, Jr.

Auditor of Public Accounts

Audit fieldwork completed -

June 25, 2003

SIMPSON COUNTY
JOE PALMA, FORMER COUNTY SHERIFF
SHERIFF'S SETTLEMENT - 2002 TAXES

January 5, 2003

<u>Charges</u>	<u>County Taxes</u>	<u>Special Taxing Districts</u>	<u>School Taxes</u>	<u>State Taxes</u>
Real Estate	\$ 916,702	\$ 482,117	\$ 2,614,297	\$ 916,882
Tangible Personal Property	129,765	71,415	373,002	548,335
Intangible Personal Property				106,166
Taxes Increased Through				
Erroneous Assessments	147	77	419	149
Franchise Corporation Taxes	54,636	29,212	155,942	
Additional Billings	129	68	367	129
Oil and Gas Property Taxes	17	9	50	18
Limestone, Sand, and Mineral Reserves	106	56	302	106
Bank Franchise Taxes	45,303			
Street Lights		7,604		
Adjusted to Sheriff's Receipt	<u>(1,072)</u>	<u>(535)</u>	<u>(3,131)</u>	<u>(1,083)</u>
Gross Chargeable to Sheriff	<u>\$ 1,145,733</u>	<u>\$ 590,023</u>	<u>\$ 3,141,248</u>	<u>\$ 1,570,702</u>
<u>Credits</u>				
Exonerations	\$ 1,057	\$ 557	\$ 3,016	\$ 2,308
Discounts	17,978	8,851	47,027	26,007
Taxes Transferred				
To Current Sheriff	116,571	60,820	326,503	128,836
Uncollected Franchise Taxes	<u>8,692</u>	<u>4,538</u>	<u>24,698</u>	
Total Credits	<u>\$ 144,298</u>	<u>\$ 74,766</u>	<u>\$ 401,244</u>	<u>\$ 157,151</u>
Taxes Collected	\$ 1,001,435	\$ 515,257	\$ 2,740,004	\$ 1,413,551
Less: Commissions *	<u>42,848</u>	<u>21,223</u>	<u>82,200</u>	<u>60,363</u>
Taxes Due	\$ 958,587	\$ 494,034	\$ 2,657,804	\$ 1,353,188
Taxes Paid	958,028	493,143	2,653,158	1,351,872
Refunds (Current and Prior Year)	<u>1,318</u>	<u>671</u>	<u>3,733</u>	<u>1,396</u>
Due Districts or (Refunds Due Sheriff)		**		
as of Completion of Fieldwork	<u>\$ (759)</u>	<u>\$ 220</u>	<u>\$ 913</u>	<u>\$ (80)</u>

The accompanying notes are an integral part of the financial statement.

SIMPSON COUNTY
JOE PALMA, FORMER COUNTY SHERIFF
SHERIFF'S SETTLEMENT - 2002 TAXES
January 5, 2003
(Continued)

* Commissions:

10% on \$10,000	\$	1,000
4.25% on \$2,650,121		112,629
4% on \$270,122		10,805
3% on \$2,740,005		82,200

** Special Taxing Districts:

Library District	\$	51
Ambulance District		<u>169</u>
Due Districts	\$	<u><u>220</u></u>

SIMPSON COUNTY
NOTES TO FINANCIAL STATEMENTS

January 5, 2003

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The Sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

B. Basis of Accounting

The financial statement has been prepared on a modified cash basis of accounting. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue which are recognized when there is proper authorization. Taxes paid are uses of revenue which are recognized when distributions are made to the taxing districts and others.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the Sheriff's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Deposits

The former Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the former Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. The former Sheriff entered into a written agreement with the depository institution and met requirements (a), (b), and (c) stated above. However, as of December 11, 2002, the collateral and FDIC insurance together did not equal or exceed the amount on deposit, leaving \$686,306 of public funds uninsured and unsecured.

SIMPSON COUNTY
 NOTES TO THE FINANCIAL STATEMENT
 January 5, 2003
 (Continued)

Note 2. Deposits

The county official's deposits are categorized below to give an indication of the level of risk assumed by the county official as of December 11, 2002.

	<u>Bank Balance</u>
FDIC Insured	\$ 100,000
Collateralized with securities held by pledging depository institution in the county official's name	3,970,000
Uncollateralized and uninsured	<u>686,306</u>
Total	<u>\$ 4,756,306</u>

Note 3. Tax Collection Period

The real and personal property tax assessments were levied as of January 1, 2002. Property taxes were billed to finance governmental services for the year ended June 30, 2002. Liens are effective when the tax bills become delinquent. The collection period for these assessments was November 14, 2002 through January 5, 2003.

Note 4. Interest Income

The former Simpson County Sheriff earned \$1,280 as interest income on 2002 taxes. As of June 25, 2003, the Sheriff owes \$294 in interest to the school district and \$680 in interest to his fee account.

COMMENTS AND RECOMMENDATIONS

SIMPSON COUNTY
JOE PALMA, FORMER COUNTY SHERIFF
COMMENTS AND RECOMMENDATIONS

January 5, 2003

1) The Former Sheriff Should Have Required Depository Institutions To Pledge Or Provide Additional Collateral Of \$686,306 To Protect Deposits

On December 11, 2002, \$686,306 of the Former Sheriff's deposits of public funds in depository institutions were uninsured and unsecured. According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with Federal Deposit Insurance Corporation insurance, equals or exceeds the amount of public funds on deposit at all times.

Joe Palma, Former County Sheriff's Response:

None.

2) The Former Sheriff Should Have Deposited Funds Intact On A Daily Basis

Technical Audit Bulletin 93-002, Section 3 requires the Sheriff to deposit funds intact on a daily basis. In addition, Technical Audit Bulletin 93-002, Section 4 requires the Sheriff to reconcile daily collections to daily deposits. During 2002 tax collections, computerized tax collection reports were not printed on a daily basis. Therefore, tax collections were not deposited on a daily basis. In addition, deposits could not be traced to the tax collection report.

Joe Palma, Former County Sheriff's Response:

None.

3) Lacks Adequate Segregation Of Duties

The former Sheriff's office has a lack of segregation of duties. Due to the entity's diversity of official operations, small size and budget restrictions the official has limited options for establishing an adequate segregation of duties. The former Sheriff could have implemented compensating controls to offset this internal control weakness.

Joe Palma, Former County Sheriff's Response:

None.

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REPORT ON COMPLIANCE
AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF THE FINANCIAL STATEMENT
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS



EDWARD B. HATCHETT, JR.
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**Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards**

We were engaged to audit the former Simpson County Sheriff's Settlement - 2002 Taxes as of January 5, 2003, and have issued our report thereon dated June 25, 2003. We did not express an opinion on the financial statements because the former Sheriff did not provide us with required management representations.

Compliance

As part of obtaining reasonable assurance about whether the former Simpson County Sheriff's Settlement - 2002 Taxes as of December 31, 2002 is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards and which are described in the accompanying comments and recommendations.

- The Former Sheriff Should Have Required Depository Institutions To Pledge Or Provide Additional Collateral Of \$686,306 To Protect Deposits
- The Former Sheriff Should Have Deposited Funds Intact On A Daily Basis



Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards
(Continued)

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the former Simpson County Sheriff's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. Reportable conditions are described in the accompanying comments and recommendations.

- The Former Sheriff Should Have Deposited Funds Intact On A Daily Basis
- Lacks Adequate Segregation Of Duties

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. We consider the reportable conditions described above to be material weaknesses.

This report is intended solely for the information and use of management and is not intended to be and should not be used by anyone other than the specified party.

Respectfully submitted,



Edward B. Hatchett, Jr.
Auditor of Public Accounts

Audit fieldwork completed -
June 25, 2003

